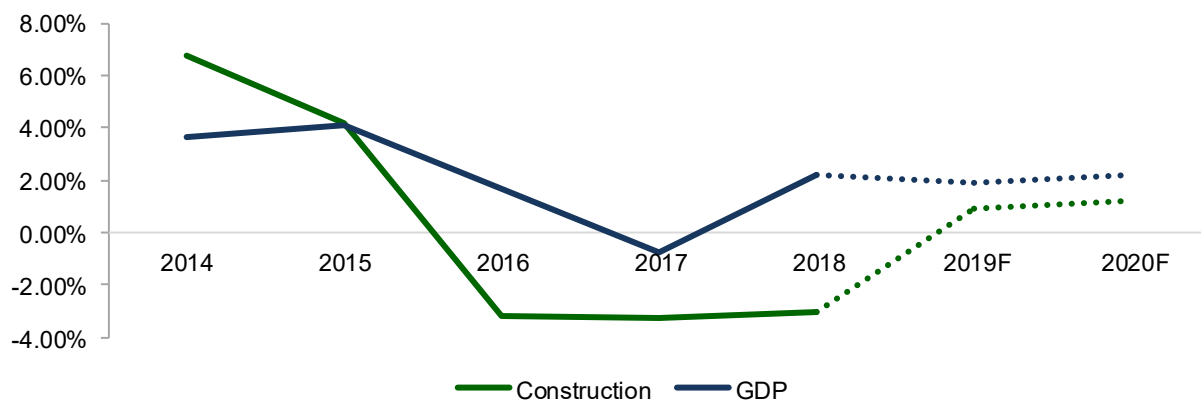




# USSABC Economic Brief: Saudi Arabian Cement Sector Looks to Rebound

The Saudi cement sector has been weighed down over the last couple of years as a result of the economic slowdown stemming from decreased oil revenues. The cement sector is significantly dependent on the construction market as it plays a pivotal role in the development, renovation, maintenance, and repair of building structures. As the pace of mega-projects began to steadily decrease after years of extraordinary growth, demand for cement dwindled while inventory levels gradually grew to record amounts. The construction sector is more susceptible to volatile swings compared to other economic activities as a contributor to GDP. As the below chart indicates, construction grew by 6.75 percent in real terms in 2014. This coincided with the decision by the government to focus on maintaining its oil production market share at the cost of lowered oil revenues, causing construction expenditures to decrease by 3.25 percent in 2017. However, recently improved economic conditions bodes well for the construction market and in turn the cement sector.

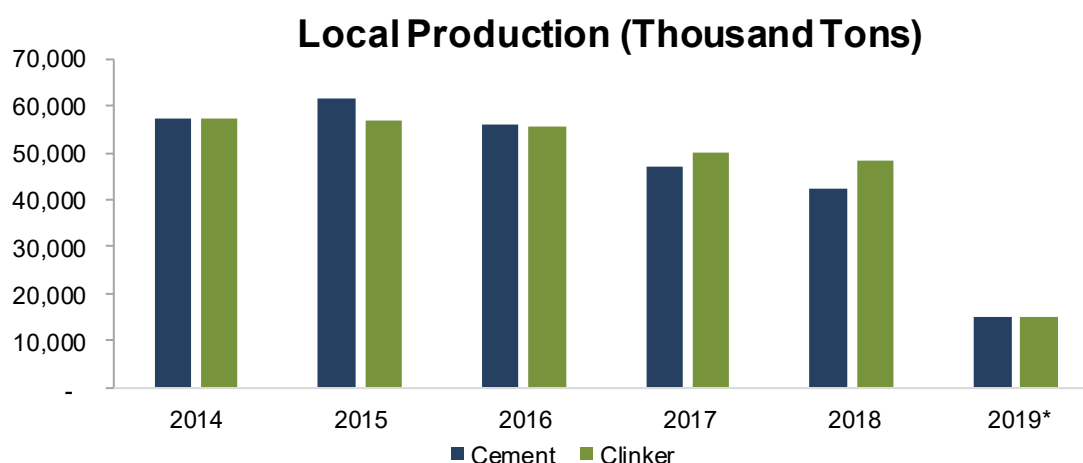
### Construction Real Growth Rates



Source: GaStat, USSABC Estimates

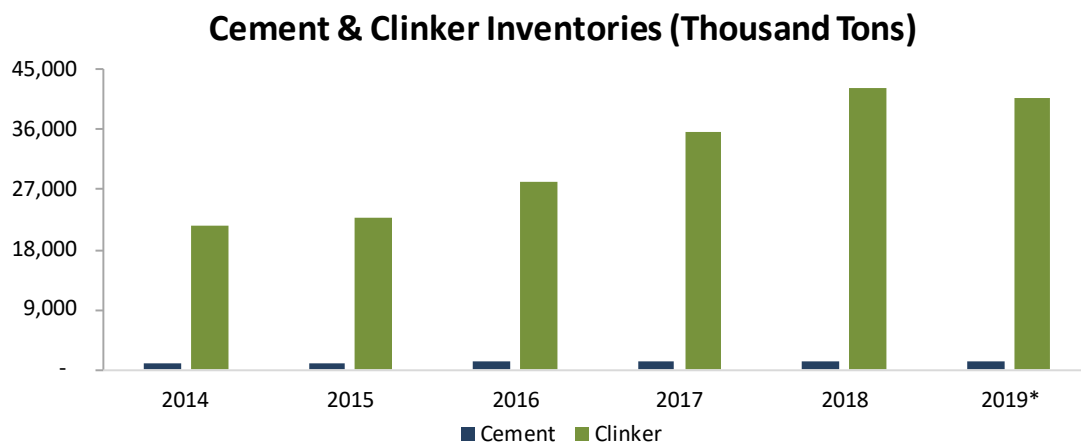
## Cement Sector Performance

The construction boom in the Kingdom contributed to record cement and clinker production to keep up with the pace of contracts awards. However, as the rate at which mega-projects were awarded declined, demand for cement began to precipitously drop. The decrease in mega-projects coupled with the reduction in energy subsidies, which increased transportation costs, impacted the profitability of local cement producers. To produce cement, clinker is ground with added active ingredients such as gypsum into a fine powder. Storing cement for long periods decreases quality and strength, making clinker the preferred storage method. Cement production decreased from 57.2 million tons in 2014 to 42.2 million tons in 2018, marking a 26 percent decline. Clinker production dropped from 57.4 million tons to 48.3 million tons during the same period, resulting in a 16 percent decline.



\*Through April 2019  
Source: Yamama Cement Company

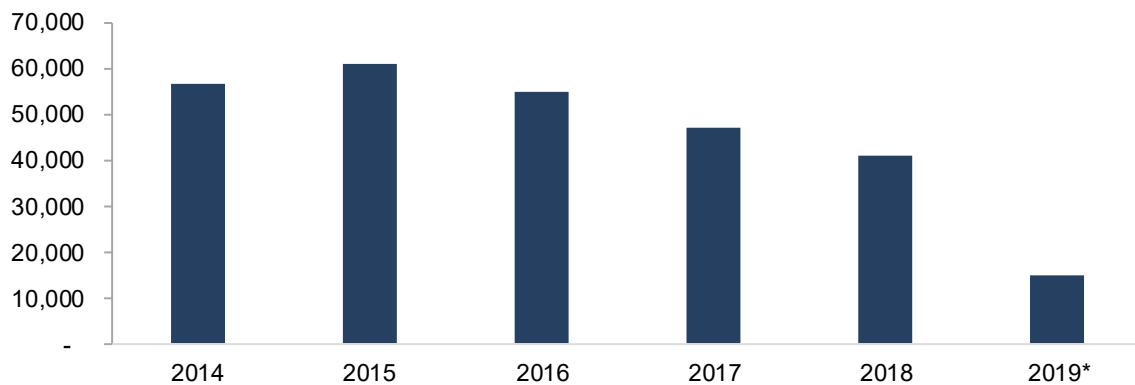
Cement and clinker inventories have markedly risen as weaker demand added to cement companies' stockpiles. This creates additional challenges for cement companies as storing clinker is more costly per ton compared to cement.



\*Through April 2019  
Source: Yamama Cement Company

While local cement sales have decreased over the last few years there have been encouraging developments thus far in 2019 that support cement companies. Local cement sales in 2014 reached 56.6 million tons but decreased to 41 million tons in 2018, marking a 28 percent decline. However, for the first four months of 2019, local cement sales reached 14.6 million tons. While the pace is slightly below 2018's there are signs that the drop in 2019 indicates sales are bottoming out with the chance of recovering as early as 2020.

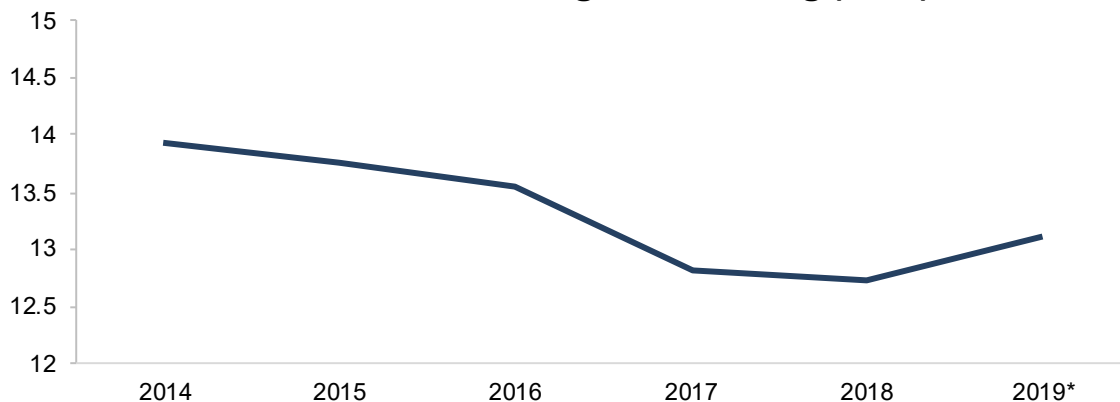
### Local Cement Sales (Thousand Tons)



\*Through April 2019  
Source: Yamama Cement Company

Local cement companies have benefitted from improved cement prices which have elevated their profitability thus far in 2019 even though demand has remained relatively flat. Cement companies, in absence of robust demand have focused on higher prices rather than maintaining market shares. Market insights indicate prices will remain elevated in 2019 regardless of subdued demand. The average price of a 50kg bag of cement climbed to SAR13.16 in April 2019 after yearly declines from 2014 through 2018.

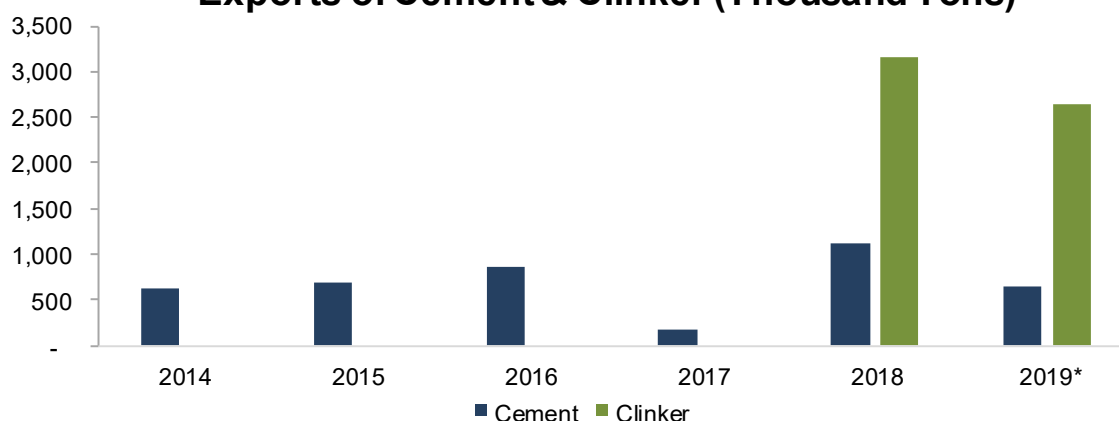
### Price of 50kg Cement Bag (SAR)



\*Through April 2019  
Source: GaStat

To alleviate slower sales, the Ministry of Commerce and Investment (MCI) lifted an 8 year export ban on cement companies in 2016. The export ban stemmed from high demand for cement locally as well as low inventory levels. The cement export tariff was originally set between SAR85-SAR133 per ton. In 2017 the MCI revised the export tariff by half to SAR43-SAR67 per ton. However, further accommodations were made in 2018 to scrap all cement export tariffs to reduce growing inventory levels. Consequently, exports of both cement and clinker significantly increased in 2018 and are on pace to grow even further in 2019. Exports of clinker through April 2019 have reached 2.6 million tons compared to 3.2 million tons in all of 2018.

### Exports of Cement & Clinker (Thousand Tons)



\*Through April 2019  
Source: Yamama Cement Company

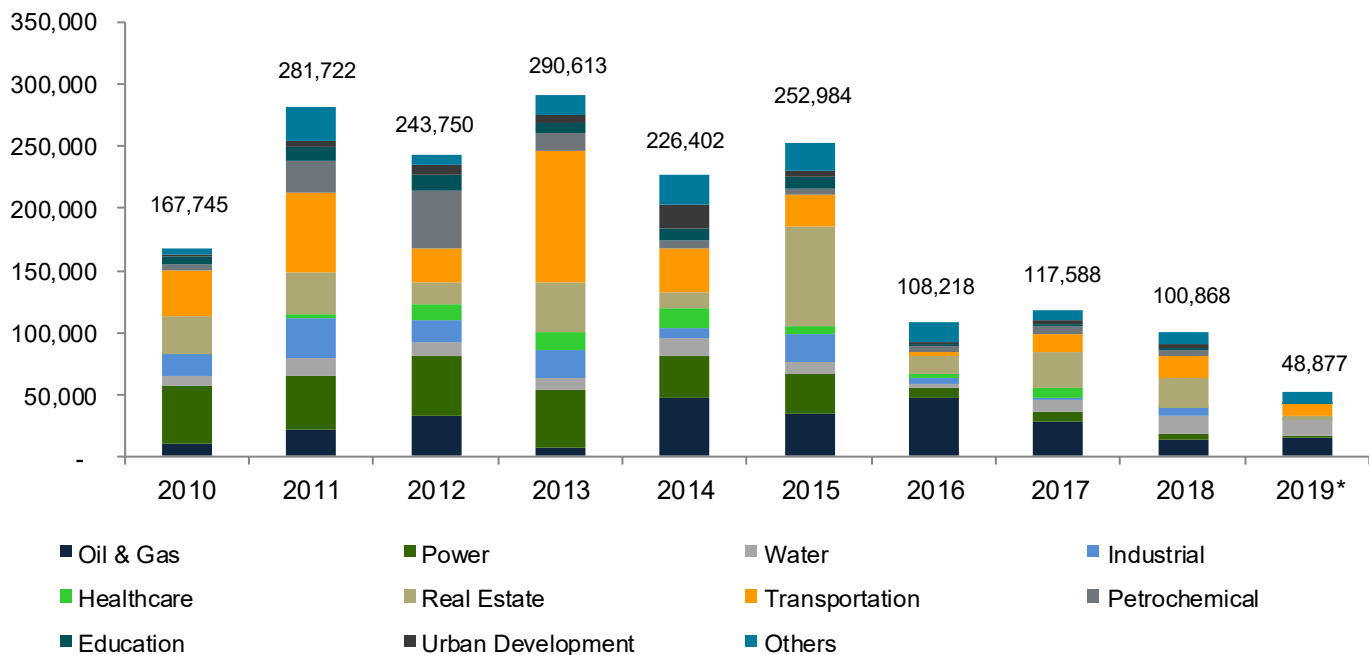
### **Cement Sector Outlook**

While the cement sector has experienced tough market conditions over the last several years, the lifting of the export ban, increases in the prices of cement, and the volume of contracts on the horizon provide positive momentum ahead. There are several factors that will enable the cement sector to rebound in the coming year and beyond. The government's budget for 2019 calls for SAR246 billion or a 20 percent increase in capital expenditures compared to 2018. This is a positive step for the cement sector as the government has earmarked increased spending across the Kingdom's infrastructure, health, education urban development, and transportation sectors. The construction of roads, bridges, hospitals, schools, and civil buildings will necessitate the usage of cement and in turn decrease the excess inventory currently stockpiled with companies.

Furthermore, as detailed in our recent report, "[USSABC Contracts Awards Index](#)" for the first quarter of 2019, the value of awarded contracts reached SAR48.9 billion. This marks the highest value of awarded contracts since the first quarter of 2015. After a depressed period of lower contract awards between 2016

and 2018, the rapid pace at which mega contracts have been awarded in Q1'19 indicate a return to a stronger, more vibrant construction sector. Unsurprisingly, the downturn in the cement sector coincides with the slowdown in contracts awards exhibiting a strong correlation between them. Consequently, this correlation will see the cement sector experience a solid recovery. The time period between a contract award and its execution can take between 6 to 18 months, depending on the magnitude of the project. This indicates that the recovery in the cement sector should be realized as early as early 2020 and into the medium to long-term.

### Value of Awarded Contracts by Year (SAR Millions)



\* Through Q1'19  
Source: Various Sources, USSABC

The contribution of the construction sector to GDP in support of these positive developments will support growth from -3.06 percent in 2018 to 0.90 percent and 1.20 percent in 2019 and 2020, respectively. In the medium to long-term, numerous mega and giga-projects will keep a steady flow of contracts on the horizon. Most notably are the NEOM, Red Sea, and the Qiddiya tourism development. The recent growth in awarded contracts coupled with larger expected projects in the near future bodes well for the cement sector's health.

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